

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-01
INR-10 NSAE-00 ICA-20 TRSE-00 XMB-04 OPIC-06
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R 292145Z AUG 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 8506
INFO AMEMBASSY BRUSSELS
AMEMBASSY PARIS

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BRUSSELS FOR USEEC
PARIS FOR USOECD
DEPT. PASS CEA, TREAS, FRB

E.O. 11652:N/A
TAGS: ECON, CA
SUBJECT: CANADIAN GNP GROWTH PICKS UP IN SECOND QUARTER.

REFS: A. CERP 0101 B. OTTAWA 3198

1. SUMMARY. CANADIAN REAL GNP GREW AT SEASONALLY ADJUSTED ANNUAL RATE OF 4.4 PERCENT IN SECOND QUARTER, UP FROM 2.9 PERCENT FIRST QUARTER GROWTH RATE. PATTERN OF GNP GROWTH SHIFTED DRAMATICALLY IN SECOND QUARTER. DOMESTIC DEMAND, PARTICULARLY PRIVATE INVESTMENT, PROVIDED MAIN IMPETUS TO GROWTH, WHILE CONTRIBUTION TO DEMAND FROM EXTERNAL SECTOR WAS NEGATIVE AS DEFICIT IN REAL GOODS AND SERVICES BALANCE INCREASED DUE TO NARROWING OF TRADE SURPLUS. DESPITE BOOST FROM SALES TAX CUT, GROWTH OF REAL CONSUMPTION DECELERATED IN QUARTER, PARTLY BECAUSE OF RISE IN SAVINGS RATIO. CURRENT GOVERNMENT SPENDING ALSO SHOWED SMALLER INCREASE, WHILE INVENTORIES UNDERWENT STRONG
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POSITIVE SWING. INFLATION RATE ACCELERATED IN QUARTER. HEAVY EMPHASIS ON DOMESTIC DEMAND IN SECOND QUARTER UNLIKELY TO BE REPEATED IN REMAINDER OF 1978. END SUMMARY.

2. GNP: REAL GNP ROSE AT SEASONALLY ADJUSTED ANNUAL RATE OF 4.4 PERCENT IN SECOND QUARTER, A SIGNIFICANT IMPROVEMENT OVER FIRST QUARTER GROWTH RATE OF 2.9 PERCENT. PATTERN OF

GROWTH SHIFTED DRAMATICALLY IN SECOND QUARTER, WITH FINAL DOMESTIC DEMAND, (WHICH ROSE AT 7.2 PERCENT ANNUAL RATE) ESPECIALLY INVESTMENT SPENDING, IN THE LEAD. CONTRIBUTION TO GROWTH FROM REAL FOREIGN BALANCE WEAKENED CONSIDERABLY DUE TO NARROWING OF TRADE SURPLUS. IN CONTRAST, FINAL DOMESTIC DEMAND ROSE AT ONLY 3.3 PERCENT ANNUAL RATE IN FIRST QUARTER WITH REAL INVESTMENT SPENDING DECLINING AT ANNUAL RATE OF 4.0 PERCENT. IN FIRST HALF OF 1978, REAL GNP ROSE AT SEASONALLY ADJUSTED ANNUAL RATE OF 4.1 PERCENT. AN EQUIVALENT PERFORMANCE IN SECOND HALF WOULD PRODUCE AVERAGE GNP GROWTH FOR YEAR OF 3.8 PERCENT OVER 1977. DETAILED DISCUSSION OF EVOLUTION OF MAIN DEMAND COMPONENTS IN SECOND QUARTER FOLLOWS BELOW.

3. CONSUMPTION: REAL CONSUMPTION SPENDING ROSE BY 0.9 PERCENT IN QUARTER, DOWN FROM FIRST QUARTER INCREASE OF 1.3 PERCENT. PERSONAL DISPOSABLE INCOME ADVANCED BY 3.1 PERCENT IN NOMINAL TERMS. INDEX OF CONSUMPTION PRICES INCREASED BY 2.1 PERCENT IN QUARTER, GIVING INCREASE OF ABOUT 1.2 PERCENT IN REAL DISPOSABLE INCOME. SINCE SAVINGS RATIO ROSE FROM FIRST QUARTER (TO 11.7 PERCENT FROM 11.5 PERCENT) GROWTH OF REAL CONSUMPTION SPENDING WAS SLIGHTLY BELOW GROWTH OF REAL DISPOSABLE INCOME. CONSUMPTION SPENDING WAS CONCENTRATED ON SEMI-DURABLES (CLOTHING, FOOTWEAR); GROWTH OF SPENDING ON DURABLES DECLINED FROM FIRST QUARTER IN SPITE OF STRONG GAINS IN UNCLASSIFIED

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PURCHASES OF AUTOS, FURNITURE AND APPLIANCES.

4. INVESTMENT: REAL GROSS FIXED CAPITAL FORMATION SHOWED A STRONG 5.1 PERCENT ADVANCE IN SECOND QUARTER, FOLLOWING 1 PERCENT DECLINE IN FIRST QUARTER. REAL PRIVATE INVESTMENT JUMPED BY 5.3 PERCENT AS 0.7 PERCENT DECLINE IN NON-RESIDENTIAL CONSTRUCTION SPENDING WAS MORE THAN OFFSET BY 5.1 PERCENT RISE IN RESIDENTIAL CONSTRUCTION AND 10.6 PERCENT SURGE IN MACHINERY/EQUIPMENT INVESTMENT. RAPID GROWTH OF RESIDENTIAL CONSTRUCTION SPENDING REFLECTS INCREASE IN WORK-IN-PLACE IN SECOND QUARTER FOLLOWING ACCELERATION OF HOUSING STARTS IN FIRST QUARTER. CONTINUED WEAKNESS OF NON-RESIDENTIAL CONSTRUCTION SPENDING ATTRIBUTABLE TO CONTINUATION OF SUBSTANTIAL EXCESS OF PRODUCTIVE CAPACITY. SUDDEN TAKE-OFF IN MACHINERY/EQUIPMENT INVESTMENT MAY BE DUE TO "BUNCHING" OF PURCHASES AND IS LIKELY TO BE TEMPORARY.

5. PROFITS: PRE-TAX PROFITS ROSE 3 PERCENT IN QUARTER AND STOOD 15.9 PERCENT ABOVE LEVEL OF SECOND QUARTER 1977. GROWTH OF PROFITS WAS STRONG IN SERVICES, TRANSPORT AND MINING SECTORS, BUT SLUGGISH IN MANUFACTURING.

6. INVENTORIES: LEVEL OF INVENTORIES ROSE BY CDOLS 430 MILLION IN SECOND QUARTER, FOLLOWING FIRST QUARTER DECLINE OF CDOLS 348 MILLION - A SWING OF CDOLS 780 MILLION WHICH PROVIDED SIGNIFICANT SUPPORT TO SECOND QUARTER GNP GROWTH. NON-FARM INVENTORIES SHIFTED FROM DECLINE OF CDOLS 84 MILLION IN FIRST QUARTER TO ACCUMULATION OF CDOLS 432 MILLION. DESPITE SHIFT TOWARD INVENTORY ACCUMULATION, RATIO OF OWNED INVENTORIES TO SHIPMENTS WAS 1.82:1 IN

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R 292145Z AUG 78
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JUNE, WELL BELOW ITS LONG TERM AVERAGE.

7. EXTERNAL SECTOR: IN CONTRAST TO DEVELOPMENTS OF RECENT PAST, EXTERNAL SECTOR WAS MAJOR SOURCE OF WEAKNESS IN SECOND QUARTER. REAL BALANCE OF TRADE IN GOODS AND SERVICES SHOWED DEFICIT OF CDOLS 4.1 BILLION IN SECOND QUARTER, A NEGATIVE SWING OF CDOLS 1.7 BILLION FROM FIRST QUARTER DEFICIT OF CDOLS 2.4 BILLION.

8. WIDENING OF REAL GOODS AND SERVICES DEFICIT WAS ENTIRELY DUE TO CDOLS 1.8 BILLION DECLINE IN REAL TRADE SURPLUS. REAL EXPORTS SHOWED QUARTERLY GAIN OF ONLY 1.3 PERCENT WITH MODEST GROWTH DUE INTER ALIA, TO (A) REACTION TO EXCEPTIONALLY STRONG RISE IN EXPORTS OF CRUDE AND FABRICATED MATERIALS IN FIRST QUARTER; (B) REDUCED STOCK-PILING IN U.S. OF CERTAIN COMMODITIES AND END OF U.S. COAL STRIKE AND, (C) STRIKES IN IRON ORE INDUSTRY IN QUEBEC - LABRADOR REGION. REAL IMPORTS GREW BY 9.4 PERCENT AS RESULT OF QUICKENING PACE OF DOMESTIC DEMAND,

PARTICULARLY FOR MACHINERY/EQUIPMENT WHICH HAS HIGH IMPORT CONTENT. IMPORT AND EXPORT PRICE INCREASES SLOWED IN QUARTER TO 1.3 PERCENT AND 1.9 PERCENT RESPECTIVELY. UNCLASSIFIED

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TIVELY. ACCORDING TO STATCAN, MODERATION IN RISE OF EXPORT/IMPORT PRICES FROM FIRST QUARTER ATTRIBUTABLE TO CHANGE IN COMMODITY COMPOSITION OF TRADE RATHER THAN TO SLOWER RISE IN PRICES OF INDIVIDUAL COMMODITIES.

9. PUBLIC SECTOR: REAL CURRENT GOVERNMENT PURCHASES OF GOODS AND SERVICES ROSE BY 1.0 PERCENT COMPARED TO 1.5 PERCENT IN FIRST QUARTER. HOWEVER, TOTAL REAL GOVERNMENT SPENDING ACCELERATED DUE TO SHARP RISE IN PUBLIC INVESTMENT. REVENUE OF ALL LEVELS OF GOVERNMENT INCREASED BY 3.2 PERCENT, FOLLOWING 2 PERCENT RISE IN FIRST QUARTER. REVENUES FROM INDIRECT TAXES DECLINED AS RESULT OF REDUCTION IN PROVINCIAL SALES TAXES IMPLEMENTED PURSUANT TO APRIL 10 GOC BUDGET. GROWTH OF NOMINAL PUBLIC SPENDING DECELERATED TO 2.4 PERCENT FROM 4.4 PERCENT RISE REGISTERED IN FIRST QUARTER AND WAS LARGELY ATTRIBUTABLE TO 0.8 PERCENT DECLINE IN FEDERAL CURRENT PURCHASES OF GOODS AND SERVICES. WITH INCREASE IN REVENUES EXCEEDING THAT OF EXPENDITURES, PUBLIC SECTOR DEFICIT (NATIONAL ACCOUNTS BASIS) SHRUNK TO CDOLS 9.7 BILLION IN SECOND QUARTER FROM FIRST QUARTER DEFICIT OF CDOLS 10.2 BILLION.

10. PRICES: INDEX OF PERSONAL CONSUMPTION PRICES ROSE BY 2.1 PERCENT, A SLIGHT ACCELERATION FROM 1.7 PERCENT RISE IN FIRST QUARTER. WHILE CUT IN PROVINCIAL SALES TAXES ACTED TO MODERATE PRICE INCREASES, BURGEONING FOOD PRICES (UP AT 26 PERCENT SEASONALLY ADJUSTED ANNUAL RATE) AND TO A LESSER EXTENT, PRICE RISES FOR MOST SERVICES, CAUSED INFLATION RATE TO QUICKEN. GNP DEFLATOR ROSE BY 2.2 PERCENT.

11. COMMENT: WITH EMPHASIS ON DOMESTIC DEMAND RELATIVE TO EXTERNAL DEMAND, PATTERN OF GROWTH IN SECOND QUARTER UNCLASSIFIED

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CONTRASTED WITH THAT IN FIRST QUARTER AND WITH THAT EXPECTED FOR YEAR AS A WHOLE. IT IS LIKELY THAT SHIFT TOWARD DOMESTIC DEMAND IS TEMPORARY. DECELERATION IN EXPORT GROWTH RESULTED IN PART FROM REDUCED STOCKPILING IN U.S. OF SOME COMMODITIES AND SOME STRIKES IN CANADIAN IRON RE SECTOR. GROWTH OF IMPORTS WAS BOOSTED BY SPURT IN MACHINERY

AND EQUIPMENT INVESTMENT WHICH IS UNLIKELY TO BE REPEATED
IN SHORT RUN. (DECLINE IN MACHINERY AND EQUIPMENT IMPORTS
IN JULY COULD IMPLY RENEWED WEAKNESS IN THIS COMPONENT OF
INVESTMENT). PICK-UP IN RESIDENTIAL CONSTRUCTION SPENDING
REFLECTED HIGH LEVEL OF HOUSING STARTS IN FIRST QUARTER.
PRECIPITOUS DROP IN HOUSING STARTS IN SECOND QUARTER
SHOULD BE FELT IN REDUCED RESIDENTIAL CONSTRUCTION SPENDING
LATER THIS YEAR. ON THE OTHER HAND, CONSUMPTION SPENDING
COULD WELL PICK UP IN THIRD QUARTER WITH POSSIBLE SPURT IN
BUYING IN ANTICIPATION OF INCREASE IN PROVINCIAL SALES
TAXES IN OCTOBER. ON BALANCE, WE EXPECT THAT EXTERNAL
SECTOR WILL LEAD GNP GROWTH FOR BALANCE OF YEAR, ALTHOUGH
POSSIBLY NOT TO DEGREE THAT IT DID IN FIRST QUARTER.

12. TABLES: GNP, FIRST AND SECOND QUARTERS 1978, BILLIONS
OF 1971 CANADIAN DOLLARS, SEASONALLY ADJUSTED AT ANNUAL
RATE (SAAR) AND PERCENTAGE CHANGE FROM PREVIOUS QUARTER
(SAAR) SHOWN IN BRACKETS ().

	----- QII 1978	QI 1978
TOTAL GNP:	125124	126496
FINAL DOMESTIC DEMAND:	128164	130476
PERSONAL CONSUMPTION:	78988	79720
V H(5.1)	(3.6)	

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GROSS FIXED INVESTMENT	26632	27984
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OF WHICH:

BUSINESS INVESTMENT:	22696	23900
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GOVERNMENT SPENDING	26480	26856
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OF WHICH:

CURRENT PURCHASES OF GOODS & SERVICES:	22544	22772
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FOREIGN BALANCE: ENDERS	- 2420	- 4112
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Secure: OPEN
Status: NATIVE
Subject: CANADIAN GNP GROWTH PICKS UP IN SECOND QUARTER.
TAGS: ECON, CA
To: STATE
Type: TE
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